The Digital Agenda for Retail Banking and Payment Companies: Why Data Holds the Key to Success

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April 2018
## Contents

### Executive Summary 3

### Digital Transformation of the Retail Banking and Payments Industry 4

### Digital and Data Trends Transforming the Industry 4

- The Growth of Online Banking 4
- Mobile Banking or “Banking on the Go” 5
- Mobile Payments Make Inroads 5
- Data-Driven Personalized Experiences 7
- Changing Customer Demographic: Millennials 7

### Transformation Agenda: Five Key Strategic Imperatives 8

- Customer 360: Data Hubs for Analytics 8
- Bank-Customer Relationship: From Products to Experiences 9
- Omnichannel to Multichannel Integration 9
- From Consumer-Aware to Context-Aware 10
- Security and Fraud Detection 11

### Summary and Next Steps 11

### Data-Driven Digital Transformation, Powered by Hitachi Vantara 12
Executive Summary

Powerful forces are reshaping the retail banking and payments industry. Customer expectations, technological capabilities, regulatory requirements, millennial demographics and new FinTech startups are converging to create an imperative for change. Banks need to get ahead of these challenges and retool if they want a win in the next era.

Banks must not only implement today’s imperatives, but also radically innovate and transform themselves for the future. In general, best-practice retail and retail banking leadership teams are focused on a core set of strategic priorities:

- Deepen relationships with customers, simplify and improve customer experience.
- Increase digital engagement by delivering differentiated experiences anywhere, anytime.
- Lead payments innovation by delivering solutions that address merchant and consumer needs.

These customer-facing priorities must be achieved while keeping cost, security and regulatory controls in check. The priorities around these include the following:

- Expense reduction initiatives and rationalized cost structure.
- A strong control environment and automated processes.
- The highest level of information-security standards.

The current environment has challenged banks with a set of disruptions impacting them from all sides. Externally, new FinTech competitors are quickly emerging in the market, often from outside the traditional banking sector, and creating new threats for traditional full-service providers. At the same time, ongoing convergence between banks and other players in areas like payments, telecommunications and retail is creating new competition and innovative business methods.

Most notably, shifts in digital, mobile, cloud, data and analytics technologies are rapidly redefining customer expectations and the way that service providers and customers interact, while dramatically cutting distribution costs to unprecedented lows. Digital and mobile banking is becoming essential. Consumers, especially millennials, view online banking as the single most important area where banks should invest, develop and automate.

Meanwhile, mobile banking and payments activity has increased nearly 50% since 2012. As a result, large, full-service banks run the risk of being outmaneuvered by their digitally oriented competitors. Placing their strategic focus on best serving customers, these emerging competitors operate and adapt more quickly, creating new tools and services that soon become industry standards.

In short, the focus on digital can represent either a threat or an opportunity. The era of branch office scale and physical presence is over; banks can no longer win through size and operational footprint alone. Instead, leaders will win by finding innovative ways to improve the customer experience, by adapting to market changes, and by accentuating both scale and flexibility. To execute against this backdrop, banks are seeking new ways to modernize their core infrastructure to accelerate business outcomes.
Digital Transformation of the Retail Banking and Payments Industry

The relationship that customers have with their bank and their finances has changed. In phase one, most traditional retail banks began offering the ability for customers to transact over the web and to go paperless.¹ Today, we are entering phase two, where customers use their smartphones or tablets to do everything from opening a new account and making payments to resolving credit card billing disputes, all without ever setting foot in a physical branch or calling a call center.

Technology is rapidly morphing from an add-on capability into a potent enabler of both customer experience and effective operations. Customers are demanding ever higher levels of service and value. Nontraditional players are challenging the status quo, and they are leading with customer-centric innovation. Meanwhile, trust in traditional financial institutions is at an all-time low.²

In the last few years, technology has rapidly evolved. Big data, cloud computing, smartphones and high-speed networks are all now commonplace, and we’ve reached a tipping point. If there is any analogy with other industries (for example, music and video distribution, retail), it would suggest that “digital” will drive huge shifts in industry value: It will compress revenues, enable new attackers, redefine service and cripple the laggards.

We are clearly in the middle of a mega-trend where digital is first focused on optimizing current products and services. The second wave, where enhanced data capture and analysis drives more targeted context-dependent customer offerings and improved services, is underway.

Technology is making it easier for customers to switch banks, making relationships much more fluid. This will drive the third wave, wherein banks and their partners develop sophisticated profiles on each of their customers. Unsurprisingly, many banks view attracting new customers as one of their top challenges over the next decade, as millennials become a larger target segment. However, banks also recognize the need to deepen their customer relationships and focus more on specific customer outcomes. Hence, enhancing customer service is the number one investment priority for banks, globally.

The pace of innovation will continue to increase, and leading banks will need to enable or leverage this innovation. All of this will accelerate the evolution of leading banks into customer-centric information and risk-management businesses.

Digital and Data Trends Transforming the Industry

Banking has been a highly regulated industry that enjoyed high barriers to entry due to regulations that restrained access for nonbank competitors. However, banks are being forced to evolve. Growth remains elusive, costs are proving hard to contain and customer expectations are evolving. Regulation and compliance are impacting business models and economics.

New digital technologies, driven by cloud, mobile, social and analytics trends, have drastically lowered entry barriers. Regulators in many countries have also relaxed controls to encourage digital innovation. As a result, many new FinTech firms, unencumbered by legacy systems, are aggressively pursuing customers by addressing their needs in new and distinct ways.

In this section, we will take a look at some of the top digital trends that retail banks and payment firms are focused on.

The Growth of Online Banking

As our world becomes more and more digital, fewer people will head to branches. It’s a well-known fact that the number of Americans foregoing branch visits is on the rise.³

¹ Paper statement delivery costs ~US$0.50, whereas electronic statement delivery costs ~US$0.011 (source: JP Morgan Chase).
² According to PwC Banking 2020 Survey, the top challenges facing banking executives include regulatory compliance, attracting new customers, increasing customer profitability, loss of trust in institutions, and new market entrants.
³ According to Mark Hamrick, senior economic analyst for Bankrate.com, “Four in 10 Americans haven’t visited a branch in 2015. That number’s risen from 18 months earlier.” If the trend holds true, even more people will be doing their banking online, on their phone, or at ATMs in 2016.
Online banking capabilities typically include the ability to:

- Conduct online banking transactions, such as viewing account balances and history, making transfers, canceling checks, viewing check images and accessing electronic statements.
- View aggregated account information.
- Receive transaction and spending alerts.
- Engage in online chat for service.
- Manage personal and business finances online and download information to accounting or tax preparation software.
- Manage user access and functions like security.

What has changed recently? The focus is shifting from features and capabilities to seamless and intuitive user experiences. Digital expectations are transforming the way customers interact with their banks. As consumers demand more personalized experiences, digital banking leaders must go beyond simply developing a “digital strategy” to increase customer retention and drive revenue growth.

**Mobile Banking or “Banking on the Go”**

Mobile banking is a relatively recent trend in the banking sector. However, the customer adoption has been staggering:

- Mobile users have ~80% more logins per week on average than online users.
- Approximately 60% of consumers rate mobile banking as an important or extremely important factor when switching banks.

Initially, mobile apps only allowed users to check their balances; compare this to the wider suite of options available today, such as mobile check deposit and peer-to-peer (P2P) bill payments. The widespread ownership of smartphones with 4G mobile Internet connections (and soon 5G) is helping to boost the popularity of mobile banking.

An important embedded capability in mobile banking that customers are increasingly using is messaging. Messaging is evolving from simple social conversations to business-related conversations. These customer service and commerce-related interactions can range from asking questions, updating account profiles and setting up new subscription plans to making reservations and transactions, and transferring money. Some analysts are now calling this “Conversational Commerce.”

**Mobile Payments Make Inroads**

Payments are at the heart of banking and have existed basically unchanged for hundreds of years. But more recently, the digitization of cash and payments has emerged as a mega trend (see Figure 1). The concept of payment is changing and evolving with the mass adoption of mobile devices. The new innovations include:

- **Mobile wallets.** The huge market penetration of smartphones is driving innovation in “mobile wallets,” which enable consumers to make payments via their mobile phones. For example, if a digitized version of a credit card is stored within a mobile wallet and used to make a payment, banks can link the card number to the user’s account and thereby authorize the transaction.

- **P2P mobile payments.** Person-to-person (P2P) mobile payments provide a means of transferring value between individuals via mobile devices, and in the case of some services, from institution to individual and vice versa.

Mobile wallet-enabled payment is a typical culmination of a successful customer experience, but it is the capabilities wrapped around this core that make for a complete and compelling in-store mobile commerce solution. PayPal, Google Wallet, Apple Pay, MasterPass and Visa Checkout are some of the new firms that have emerged in recent years to attack the mobile payment market.
As customers seek faster checkouts and frictionless commerce, “invisible payment” is becoming a new trend. “Invisible” (or automatic) payments embed payments into mobile apps to be automatically triggered upon consumption of a service. Paying for Uber cars is an example of an invisible payment.

Walmart Pay recently launched its mobile payments app, which mimics an eCommerce transaction at checkout: It links the consumer’s app to a QR code that not only triggers payment but also applies coupons, promotions, and Savings Catcher and gift card balances. The phone can be inside a consumer’s pocket or purse. It isn’t even material to the “checkout” once the shopper has been checked in via the app.

Rapid, significant and disruptive technological changes, such as mobile order-ahead and peer-to-peer, continue to impact the payments industry. These changes include developments in payment card tokenization, ecommerce (for example, social commerce), mobile, virtual currencies like Bitcoin, near-field communication (NFC) and other proximity payment devices, such as contactless payments.

As nonbank players such as PayPal continue to strive to become integral in customers’ everyday lives, they could become more of a threat to banks. PayPal offers services similar to traditional financial institutions but consumers typically use them differently. PayPal users can store money in their accounts (or link to a credit card on file) and then use the service to transfer money and buy products either in-store or online. And PayPal also provides loans and credit cards through partner banks.

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**Figure 1. Example of a Digital Payments Architecture**

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Data-Driven Personalized Experiences

Millions of banking interactions are occurring on the web, on mobile devices, on social media, at ATMs and at branch and call centers. This vast store of information is being constantly aggregated and analyzed so banks can deliver relevant real-time customer experiences.

Transaction, preference and social data, as well as the creative use of that data to identify patterns, has the ability to inspire the frequency of use that builds preference, engagement and loyalty.

The ability to leverage data and design the right contextual experience to target mobile and multiscreen-experience customers is key. History indicates that there has been no shortage of new digital banks, some started by entrepreneurs and others backed by major traditional banks, that have failed to take off due to low customer adoption.

Delivering great customer experience and living up to the needs of digital banking are some of the business challenges that banks face today. Digital teams at retail banks are racing to infuse insights from data into their omni-channel experiences to provide personalized, relevant, preapproved financial product offers as well as to deliver spending-related offers through digital wallets.

Changing Customer Demographic: Millennials

Millennials — born between 1980 and 2000 — are both the 20th century’s last generation and mankind’s first truly digital one. Millennials are fast becoming an important demographic for retail banks as they look for growth. They are also putting pressure on banks to change by improving online channels.

Figure 2 illustrates the segmentation of the banking customer base.

**Figure 2. Breakdown of Customer Segments**

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</thead>
<tbody>
<tr>
<td>Year Most of Generation 18-33 Years Old</td>
<td>1963</td>
<td>1980</td>
<td>1998</td>
<td>2014</td>
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**Summary**
- Retirees: Grew up during Great Depression, Fought in WWII, the “war to end all wars.” Went to college on G.I. Bill, Raised “nuclear” families in time of great prosperity and Cold War.
- Baby Boomers: Grew up during time of idealism with TV and car for every suburban home, Apollo, Civil Rights, Women’s Liberation, Disillusionment set in with assassination of JFK, Vietnam War, Watergate and increase in divorce rates.
- Gen X: Grew up during time of change politically, socially and economically, Experienced end of the Cold War, Reagonomics, shift from manufacturing to services economy, and AIDS epidemic, Rise of cable TV and PCs.
- Millennials: Grew up during digital era with internet, mobile computing, social media and streaming media on iPhones, Experiencing time of rising globalization, diversity in race and lifestyle, 9/11, war on terror, mass murder in schools and the Great Recession.

**Core Values**
- Disciple, Dedication, Family focus, Patriotism
- Anything is possible, Equal opportunity, Question authority, Personal gratification
- Independent, Pragmatic, Entrepreneurial, Self reliance
- Globally minded, Optimistic, Tolerant

**Work and Life Balance**
- Work hard for job security, Climb corporate ladder, Family time not first on list
- Work/life balance important, Don’t want to repeat Boomer parents’ workaholic lifestyles
- Globally minded, Optimistic, Tolerant

**Technology**
- Have assimilated in order to keep in touch and stay informed
- Use technology as needed for work and increasingly to stay in touch through social media such as Facebook
- Technology assimilated seamlessly into day-to-day life
- Technology is integral, Early adopters who move technology forward

**Financial Approach**
- Save, save, save
- Buy now, pay later
- Cautious, conservative
- Earn to spend
Millennials expect that banking will, and should, change and serve them differently than it did their parents’ generation. For these digital natives, the smartphone is not only ubiquitous, but also their primary screen. For instance, the best way for banks to contact millennials is through social media and chat. The worst way is over the telephone, since few answer it.

Millennials are looking for new capabilities from their banks. They want the institution to act as an “overall financial hub” or a personal financial dashboard for them. They are expecting the bank to advise them on how much to save and budget. They want more self-service functionality and yet also have the convenience of being able to reach a human via chat if there is a problem.

The challenge is being able to balance automation and personal touch. Interestingly, some banks are responding to declining branch visits from millennials by raising cost per transaction at branches. This, in turn, reduces traffic, resulting in more branch closures. Clearly, large banks, community banks, and credit unions need to redefine the service relationship they have with the millennial segment.

Transformation Agenda: Five Key Strategic Imperatives

As we highlighted in the previous section, powerful forces are transforming the retail banking and payments industry. But banks are no strangers to technology-led transformation. Banks have always invested in the development of more sophisticated technology capabilities in order to improve customer service, payment operations and client service, as well as to reduce risk, lower costs and establish a competitive advantage.

Each bank needs to develop a clear growth strategy to deal with commoditization and the competitive landscape. They need to decide whether to lead, to follow fast, or to manage defensively while putting off change. They need to create agility and optionality to adapt to rapid change and future uncertainty. Whatever the chosen strategy, success will come from the right balance of the following imperatives:

- Customer 360: Data Hubs for Analytics.
- From Products to Experiences.
- Omnichannel and Multichannel Integration.
- From Consumer-Aware to Context-Aware.
- Security and Fraud Detection.

Customer 360: Data Hubs for Analytics

Banking is an industry that generates enormous amounts of relevant customer data: transactions, call center and ATM interactions, new account openings, account funding, online logs and social media comments.

In their customer data hubs, leading banks are aggregating every data point, from socio-demographic information to spending habits. They combine attrition tendencies, product and communications preferences, affinity scores and up-to-the-millisecond intelligence on digital behavior and context.

The need to have a holistic view of the customer has become a priority, especially for those processes that are customer-facing, such as cross-sell and upsell, complaint handling, service requests and so on. For both customer personalization of services and effective risk profiling, more longitudinal information about the customer has the potential to add value.

The key challenges banks continue to face are the effective aggregation of relevant customer data on a timeline and the conducting of descriptive, predictive and prescriptive analytics on top of the data hubs. Elements of these challenges include the following:
Unique customer ID. Today, one of the most fundamental problems in a bank is customer identity management. This is basically having multiple instances of data that represent a single entity with multiple records. For example, a customer may have a credit card, a housing loan and a fixed deposit. A bank has different systems for selling credit cards, investment products and loans; a customer might own all the three types of products, but unless the bank has a way to resolve the multiple identities across all the systems, it will end up selling or underwriting loans based on incorrect information.

Householding. Householding is the process of identifying connected individuals or households in a bank’s product portfolio. This is important because it gives them a chance to run campaigns involving households rather than individual customers. It also gives them a chance to avoid making, say, credit card offers when they have a view of the households of risky customers.

Contactability. Contactability is defined as the ability of the customer service team to connect with the customer through messaging, email or phone as well as via social media. This is a very important attribute of customer data. Better contactability leads to faster customer interaction, thus helping sales agents in upsell and cross-sell as well as in the faster resolution of issues.

Relationships. Relationships are the list of all active and inactive relationships of a customer with the bank, such as credit cards, car loans and mortgages.

Bank-Customer Relationship: From Products to Experiences

A customer may have multiple product relationships with a bank, including checking accounts, savings accounts, credit cards and loans. Most banks have attempted to create optimized relationships, but only within their product silo. This is changing as banks develop the ability to manage individual customer profiles that can be leveraged to create unique experiences.

A more personalized experience for customers is now a requirement. The digital environment has revealed that what truly drives loyalty is the quality of the simplified, differentiated and personalized experiences that customers have before, during and after an interaction. Their loyalty to an experience, as opposed to a company or product, is evident in several research findings:

- 65% of consumers use online channels, not primarily for price advantages, but for convenience, speed, the quality of information provided, and access to a broader range of choices.
- 65% find “being promised one thing and delivered something else” the most frustrating experience they can have with a company.
- 65% (nearly 80% in emerging markets) have switched at least one provider in the past year because of poor service.

Attrition, also commonly referred to as churn rate, is often the result of a poor experience. Consumers evaluate providers foremost on the experience that a bank provides, more so than on the products or services. It’s time for banks to acknowledge that loyalty is neither permanent nor under their control. Digital has confirmed the need to delight or surprise customers on an ongoing basis. Every experience makes a difference. And satisfying experiences, delivered over time, are what build long-term relationships and drive profitable growth.

Omnichannel to Multichannel Integration

Smartphones are making it easier for customers to “self-serve.” Banks are responding to this by enabling better multichannel transactions: online, ATM, tablet and smartphone. This also requires enabling cross-channel integration, where a transaction could be started on the smartphone but finished in a branch.

The multichannel approach came to the fore several years ago, when banks launched online platforms and encouraged customers to use call centers for their everyday banking needs. The number of touch points increased, but with expansion came more complicated and siloed IT systems.
Additional channels were bolted on to legacy platforms, but many banks have struggled to offer a joined-up approach to servicing customers. As consumers ourselves, we have all experienced this fragmented experience. For example, how many times have you been offered an unwanted loan by your branch and subsequently been targeted with the same question while carrying out your online banking?

From the customer’s perspective, omnichannel banking continues to offer access to financial services across a variety of channels and introduces more consistent interactions with the banking brand across the various touch points. The bank is able to analyze the information feeding in from different channels so that it can build up a detailed and accurate picture of the customer’s preferences and behavior.

Today’s consumers are increasingly sophisticated and are accustomed to targeted offerings from companies (such as Amazon) that make relevant purchasing suggestions regardless of the device in use. So it comes as no surprise that these same customers have come to expect similar service from their bank.

In summary, millennials and other digitally minded consumers are forcing financial institutions to rethink the way they do business. These consumers want to bank when and how it suits them. With omnichannel banking, customers expect a consistent experience, whether they access their bank via mobile, tablet or visiting a branch in person. If the banks don’t step up and provide this omnichannel experience, there are plenty of other institutions that, unencumbered by legacy systems and cultures, are relishing the opportunity.

**From Consumer-Aware to Context-Aware**

The rapid innovations in digital assets and channel technology have far-reaching implications for banks, which need to adapt their offerings not only to the evolving technology but also to the corresponding shift in consumer expectations. Reducing the cost-to-serve using context-specific intelligence is a key priority for banks.

Armed with the awareness that mining user data is critical for a service provider, the digital-centric customer of today is more open to sharing information but with the expectation that the information will be used to deliver a customized and context-aware experience. Instances of these include the location-based offers powered by multivariate testing techniques, data science algorithms and advanced data analytics.

However, a context-aware experience is not limited to location-based offers or promotions. The user now expects the mobile device to be an extension of his or her identity and personality. This presents an opportunity for service providers to offer a truly intuitive and context-aware experience, using the data stored in the user’s device, relationships and transaction history. Technically, this requires scaling data pipelines (see Figure 3 below) to accommodate multiple data sources, volumes and types.

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*Research from Google has shown that 46% of people managing their finances online switch between devices before completing the activity.*

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Security and Fraud Detection

Consumers love the convenience of digital banking and mobile payments, but remain uneasy about the security of their electronic transactions, including deposits, passwords and logins. This leaves financial institutions with the difficult task of delivering transaction technologies that are as battle-hardened as razor wire, and as easy to use as a butter knife.

The mobile app is fast becoming the banking vehicle of choice, not only for millennials, but also for “fast followers” in the baby boomer demographic. Monitoring and securing the mobile app when it’s used as, say, a cardless ATM, is becoming a huge battlefield between hackers and the banks. Real-time fraud alert is another critical capability requirement.

There is an opportunity to link data and analytics to the flow of payments, such as e-wallets, mobile and digital currencies. This approach is frequently cited as a probable and attractive evolution of payment propositions. It benefits both parties involved in the transaction and is as a means of meeting “Know Your Customer” (KYC) requirements linked to various regulatory anti-money-laundering laws.

Hackers are getting more ambitious, spending longer on penetration attacks and demonstrating greater sophistication, and the rewards they’re reaping are larger than ever. To combat this, banks are increasing their technology budgets aimed at innovation, encryption and security.7

Summary and Next Steps

The banking and payments sector is in the midst of rapid evolution driven by a sharp uptick in innovation, changing patterns in consumer consumption, and a number of strategic growth initiatives and shifts in market conditions.

New cloud, mobile and analytics technologies have both enabled and in turn been fueled by a huge influx of new providers and products, all vying to enter the payments space. This development has contributed to an element of “unbundling” of financial services, which are increasingly exposed to growing competition, and to non-banks offering attractive, cost-saving solutions that aim to provide better overall experiences for clients.

To survive and thrive, banks have to innovate (see Figure 4). A true, sustainable digital bank business model means that the bank optimizes its customer interactions, products, processes and data around digital technologies. Successful digital banks are appealing on the front end and are also digitally efficient on the back end. They use mobile and digital technologies to lower the costs to serve; at the same time, these technologies are also used to enhance higher touch services.

Figure 4. Strategic IT Initiatives in Typical Retail Banking and Payments Provider

7 JPMorgan plans to increase its technology spending up to US$9.4 billion in FY16 compared to US$9.2 billion spent in FY15. It plans to allocate around 40% of that budget to innovations, compared to the previous 30%. The bank also plans to spend US$600 million on
Modernization of IT processes, people, applications and infrastructure is a key foundational enabler of every digital transformation. In addition to introducing new technologies and offerings, banks must phase out outdated applications and infrastructure. If they are unable to do so on a cost-effective basis, they could experience reduced profits or face irrelevance.

Digital transformation isn’t an end goal; for banks, it’s a continuous journey. As customers shift their behavior and move more toward digital solutions, banks will need to evolve their digital strategy.

**Data-Driven Digital Transformation, Powered by Hitachi Vantara**

Organizational transformation in today’s volatile market is at the core of business survival. While business leaders expect IT to remain focused on results, enable innovation and provide continual improvements, it’s not enough to rely solely on technology to transform the business.

In the retail banking and payments industry, this value realization game plan translates into the following outcomes:

- Achieve cost savings and accelerate time to market by rethinking operations and processes.
- Increase customer loyalty and grow revenue through improved customer experience.
- Uncover new revenue streams and reach new markets with new business models.

Accomplishing this begins by transforming IT. A transformative organization must do the following:

- Modernize their technology stack to address how data are managed and governed.
- Integrate siloed application platforms to centralize data to address mobility and analytics.
- Deploy automated tools for development and operations.
- Use data analytics for continual improvements, balanced utilization and new opportunities.

Successful digital business transformations are entirely dependent upon taking a strategic approach to your enterprise data. If you are like most companies, you have multiple data silos. Enterprise transformation starts with bringing those disparate data sets, whether structured, unstructured or machine-generated, into a single data strategy. At Hitachi Vantara, we offer our customers an integrated and secure way to manage, govern, mobilize, analyze and ultimately turn those data into insights that create new opportunities for industry-specific use cases.

Figure 5 illustrates our data-driven digital transformation model, depicting the notion that data are the engine behind a transformation, but change quickly. With data continuing to originate from various sources, and presented in evolving types, ensuring the veracity of your data is key to monetizing them and is the basis of your market leadership and ability to achieve your transformational outcomes.

A call to us to learn more about each element of our recommended data strategy could be the difference between success and failure.
Figure 5. Data-Driven Digital Transformation Model From Hitachi Vantara